

Natural Foods Supermarkets Gaining in Popularity

Phil R. Kaufman
(202) 694-5389
pkaufman@econ.ag.gov

Natural foods supermarkets are achieving record growth as they gain acceptance from more and more health-oriented consumers. The outgrowth of the earlier health-food stores, natural foods supermarkets have expanded in size to accommodate all the departments of a traditional supermarket, including prepared foods and meals.

"Natural foods" are minimally processed and free of artificial ingredients, preservatives, and other non-naturally occurring chemicals. Although health and natural foods stores have long existed as a niche market in food retailing, they typically offered a more limited range of health foods and related products, such as nutrition supplements, partly because of their smaller size, but also to meet the needs of customers seeking pesticide-free produce, meatless food sources, or produce for restricted diets.

Natural food supermarkets aim to meet the needs of a broader consumer segment interested in improving the nutritional value of their diet to achieve greater health benefits. Interest in natural and

organic food products has been fueled in part by the increasing awareness of the links between diet and health, rising incomes, and the aging of the "baby-boom" generation born between 1946 and 1964. The larger size of natural foods supermarkets, measured in square feet of floor space, provides greatly expanded variety and accommodates all the departments of a traditional supermarket, including environmentally friendly nonfood products. Prepared foods and meals address the needs of time-pressured households having a preference for natural ingredients. Consumers also benefit from the convenience of knowing that most of the product offerings are either certified organic or are made from natural ingredients.

A Small but Growing Market

According to *Health Food Business Annual Survey of Health Food Stores*, the health food store industry has achieved considerable gains over the past several years, reaching sales of an estimated \$8.4 billion in 1997, up from \$7.6 billion in 1996. Chains such as Whole Foods Market and Wild Oats—the two largest retailers

in the segment—were responsible for an estimated \$2.3 billion in 1997 sales.

Natural foods supermarkets are making significant contributions to the expansion and accessibility of natural foods by pursuing aggressive growth strategies and by opening larger, full-service stores. Prior to the early 1990's, relatively few natural food stores in the United States were large enough to meet the supermarket definition of \$2.5 million or more in annual sales (in 1985 dollars, adjusted for inflation in subsequent years). Retailers were mostly independents operating fewer than 10 outlets in a single city. Since then, the number of multi-store, multicity natural foods supermarket firms has grown. By 1993, Whole Foods Market operated 30 natural foods supermarkets in eight States. In metropolitan Washington, DC, Fresh Fields Markets opened several supermarkets and later opened stores in Chicago, New York, and Philadelphia to number 22 stores by 1996. Mrs. Gooch's Natural Food Markets operated seven stores in the Los Angeles area in 1993.

The author is an agricultural economist with the Food and Rural Economics Division, Economic Research Service, USDA.

Consolidation has since reduced the number of multistore retailers despite rapid sales growth. Wild Oats Markets operated 11 natural foods stores in 1993, and has since grown—largely through acquisitions of other existing operations. In July 1996, it acquired Alfalfa's, a chain of 11 natural food supermarkets operating in Colorado, New Mexico, Washington, and Canada, with sales of \$90 million. Wild Oats Community Markets is the second-largest retailer in the segment, operating 54 stores in 12 States and Canada, with sales of \$311 million in 1998.

A similar strategy was pursued by Whole Foods Market, which began operations in 1980, and grew rapidly through acquisitions. In October 1992, it purchased Bread & Circus, which operated six natural foods supermarkets in Massachusetts and Rhode Island, followed by the acquisition of Mrs. Gooch's Natural Food Markets with seven stores in Los Angeles, CA. In 1996, it acquired Fresh Fields, a chain of 22 upscale natural foods supermarkets located in the Mid-Atlantic and Midwest. As a result of these activities, coupled with smaller store purchases and new store openings, Whole Foods operated 75 supermarkets in 17 States, generating sales of \$1.05 billion in 1997.

The growth of natural foods supermarkets has taken place mostly in urban central cities and their surrounding suburban areas. These markets range in size from Boulder, CO, to Los Angeles, CA. Demographics likely play a key factor in deciding where to locate new stores. Because natural food products generally cost more, retailers must price them accordingly in order to cover store operating costs. The price premiums often associated with natural foods dictate that stores be located near households with above-average incomes, which are generally found in major metropolitan areas.

Store Focus Differs, but Becoming More "Mainstream"

Although natural foods supermarkets are similar to their traditional counterparts by virtue of the complete coverage of food and non-food departments, and by meeting minimum sales requirements, differences in the importance of food categories (measured by share of store sales) often vary greatly (table 1). Aside from the produce department, bulk foods are very limited in traditional supermarkets, yet many natural foods shoppers are accustomed to purchasing grains, seeds, cereals, and dried fruits in this manner. Produce receives a greater share of natural food shoppers' dollars, as expected, while only about one-third as much fresh meat, seafood, and poultry are sold in natural foods supermarkets. The importance of packaged foods in natural foods stores is comparable to that of traditional supermarkets, however. Evidence of changing preferences among natural foods supermarket shoppers can be seen in the sizable share of sales of prepared food, outpacing the share of sales found in traditional supermarkets.

Among format types, natural food supermarkets (which are not normally classified separately) would account for a relatively small share of total supermarket sales (table 2). However, surveys indicate interest in natural and organic food products is becoming more widespread. Consumer interest in alternatives to traditional supermarket offerings, coupled with the expected approval of Federal organic-certification standards, will likely result in natural food products capturing a larger share of the mainstream consumers' food dollars.

Evidence of the changes in consumer preferences can be found in the efforts of traditional supermarkets to introduce more organically grown foods, including packaged products. Some of the largest food retailers across the country are expanding natural foods offerings in their stores. For example, Albertson's, A&P, and Publix have announced that they will offer processed organic foods—such as frozen entrees, sauces, dressings, tortilla chips, pretzels, and syrups—in addition to organic produce items. Traditional retailers are also experimenting with different ways to display natural foods, whether

Table 1
Major Differences in Sales by Natural Foods and Traditional Supermarkets

Food category	Natural foods supermarkets	Traditional supermarkets
Percent of sales		
Bulk foods	8.0	0.1
Produce	19.0	14.2
Beverages	5.0	6.7
Meat and seafood	6.0	19.4
Packaged products	32.0	28.5
Refrigerated and frozen foods	13.0	14.9
Snacks	4.0	3.3
Bakery	3.0	4.3
Foodservice	10.0	8.6

Source: *Food Institute Weekly Digest*, 5/12/97, and *Supermarket Business*, Sept. 1997.

Table 2

Natural Foods Supermarkets Are the Smallest Supermarkets, in Both Numbers and Share of Sales

Supermarket format	Share of supermarkets		Share of supermarket sales	
	1997	1980	1997	1980
	Percent		Percent	
Natural foods	0.7	NA	0.7	NA
Conventional	43.8	85.0	18.5	73.1
Superstore	30.8	8.9	43.2	17.7
Combination	12.0	.9	21.0	4.0
Warehouse/limited assortment	9.5	4.7	7.2	4.2
Superwarehouse	2.1	.5	3.9	1.0
Hypermarket	1.0	NA	5.4	NA

Notes: NA = Not applicable. Data may not sum to 100 due to rounding. A natural foods supermarket is a full-line grocery store meeting minimum annual sales for a supermarket, and specializing in natural and organic foods. A conventional supermarket is a full-line grocery store, primarily self-service in operation, having minimum annual sales of \$2.5 million or more in 1985 dollars, and adjusted for inflation in subsequent years. A superstore supermarket contains a greater variety of products than do conventional supermarkets, including specialty, services, and considerable nonfood (general merchandise) products. A combination supermarket contains a pharmacy and a nonprescription drug department offering extensive personal care products. A warehouse supermarket contains limited product variety and fewer store services than provided by conventional supermarkets, and incorporates bulk stocking and shelving practices. A superwarehouse supermarket is a larger warehouse store that offers expanded product variety and often service meat, deli, or seafood departments. A hypermarket supermarket is a very large supermarket offering a greater variety of general merchandise—like clothes, hardware, and seasonal goods—and personal care products than other format types.

mixed in with conventional counterparts, or grouped together with distinct labeling and signs in the aisles. Although many traditional supermarket retailers want to meet the needs of consumers seeking natural foods, the selection of products is often governed by the ability of suppliers to distribute across a region or multiple regions, to keep retail price premiums to a minimum, and to meet high quality standards.

Natural foods supermarkets are looking to continued sales growth. Both Whole Foods Markets and Wild Oats Community Markets have ambitious new store and acquisition plans. Wild Oats added 13 stores and entered 4 new States in 1997, and has contracts to open 8 new locations in 1998. Similarly, Whole Foods Markets aims to add 25 new stores by 2000, and by 2003, it plans to operate more than 140 natural foods supermarkets in metropolitan areas across the United States. ■